Financial Strategy 2024-2034

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Financial strategy

The short story

We expect rates to increase by 15.09% after growth in the rating base, in year one (2024/25), and debt to increase from $25.7 million in year one to a peak of $53 million in 2033/34. Debt is forecast to remain within our Council imposed limit of 15% of total assets. We anticipate that an operating surplus will be made each year during the planning period, reflecting our need to service that debt.

The demand we are facing

Maintaining and upgrading our infrastructure accounts for over half of our annual operating expenditure, and most of Council's capital expenditure. This includes roads, footpaths, wastewater, our urban water supply, and stormwater.

Our infrastructure is essential to the health, safety, and transport requirements of the district, and has a significant impact on the physical environment. We need to strike the right balance between ensuring we have reliable, quality infrastructure, while weighing up the needs of our growing community, and how our infrastructure will be funded.

Key projects and levels of service that need funding in this Long-Term Plan are:

- Improving our maintenance and renewals of the roading network
- Completing the remainder of Cyclones Gabrielle and Hale emergency works on our roads
- Upgrading the intake of our wastewater plant
- Delivering resilience across our community including the development of new trails and footpaths
- The demand for services with population growth
- The impact of climate change and extreme weather events
- The risks to and resilience of our assets
- The response to changing regulatory requirements from central government

When considering how to share these costs across our community, the Council has applied the following principles:

- Be fair to our ratepayers and customers
- Maintain service delivery and if required, meet increasing demand
- Balance the budget – planned revenue equals planned expenditure
- Be good stewards of our assets and infrastructure, and of our funds
- Spread the cost of our assets across their useful lives

The economic climate is regaining stability, but global financial and geopolitical issues continue. Consequently, the Council has allowed for limited growth in the rating base to reduce from to the last ten-year period of 1.2 percent to between 0.75 percent per annum for year one, reducing to 0.50 percent for years two and three and staying at a level of 0.25 for the remainder of the ten-year period.

Costs of meeting demand

Capital Investment

Capital investment or expenditure is for purchasing, building, replacing, or developing the district's assets, such as roads, parks, underground pipes, and buildings. For each major infrastructure network (water, sewerage, stormwater, and roads) asset management plans are in place. These are key planning tools for the maintenance, renewal, and development of assets.

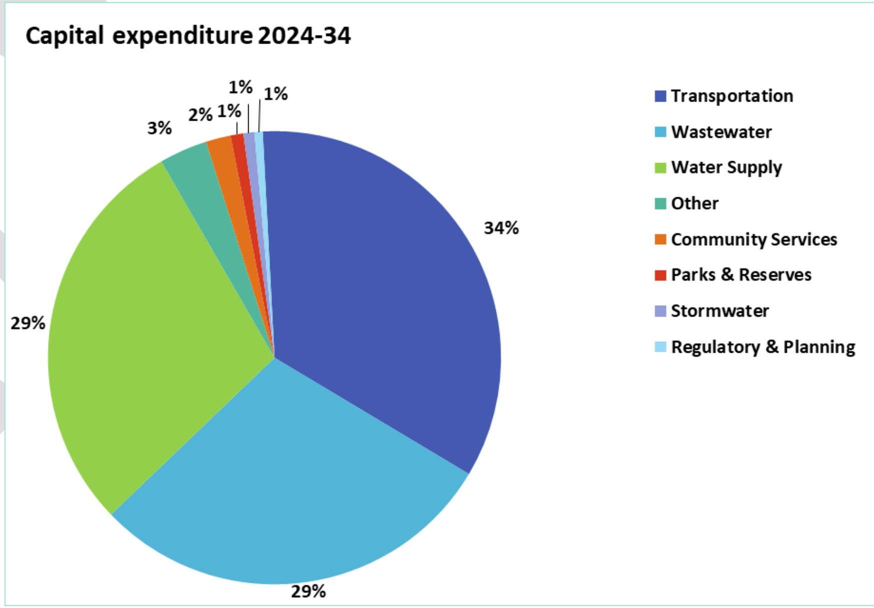
The assets managed by the Council are forecast to grow from $268 million to $320 million over the ten years of this plan.

The key capital projects over the ten-year plan are as follows:

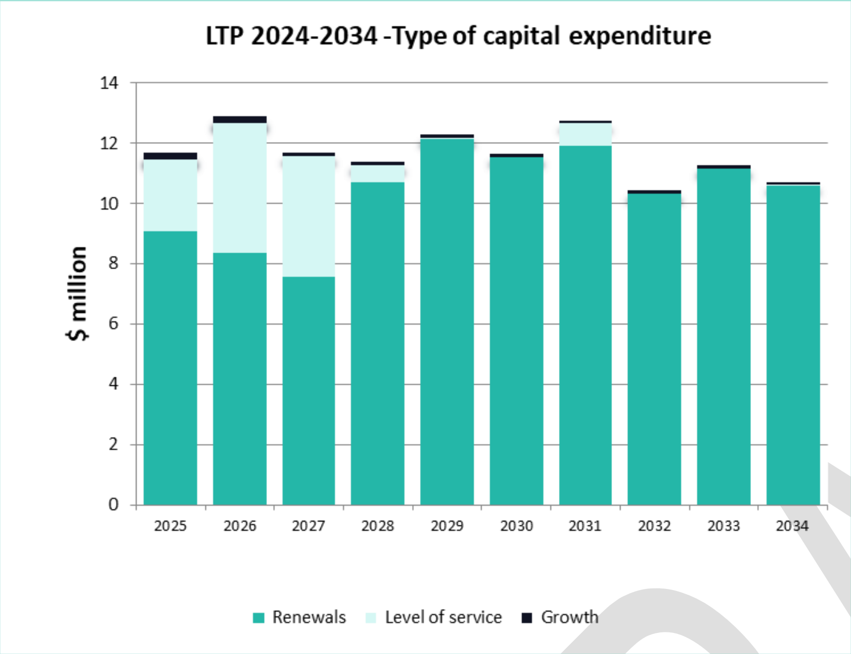
- Water Treatment intake- improve our treatment of wastewater, including grit and fat removal, new primary sedimentation tank and foul air treatment, $6 million over three years
- Transportation – invest in resurfacing and rehabilitation our roads, also referred to as 'pavement renewals' to provide longevity in the condition of our roads, completion of our emergency works following the damage caused by Cyclones Gabrielle and Hale and maintaining our existing levels of service for road maintenance.

The Council will spend nearly $116.7 million on capital expenditure over the next ten years ($11.7m in 2024/25). The chart below provides a breakdown by major group of activities. The largest share of the capital spend is on transportation ($40.1 million or 34%) followed by wastewater ($34.1 million or 29%) and water supply ($33.6 million or 29%).

The chart below breaks down capital expenditure between renewal of existing assets, responding to, or anticipating growth in demand, and improving levels of service.



As shown in the chart, a large portion of the capital expenditure forecasted for the next ten years is predominantly in levels of renewals and maintaining current levels of service of our assets for years one to three and for limited growth for the remaining years.



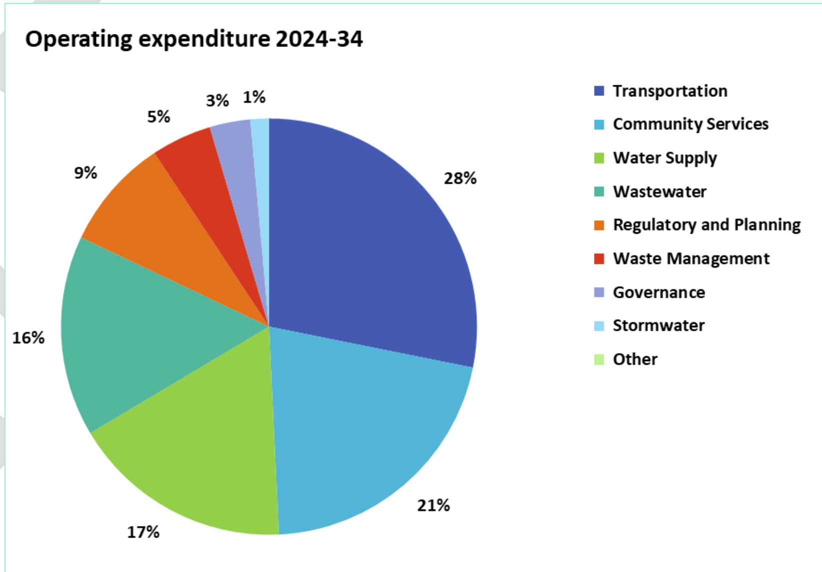
The Draft Infrastructure Strategy provides further details on Levels of Service (pages 6 and 7.)

We are operating in a world of limited funding and difficult investment trade-offs. This dynamic and changing environment within which we manage infrastructure assets means that we need to revisit assumptions and forecasts as new information comes to hand.

The criticality and condition of our networks has been a key driver behind investment and management of our pipe networks. In order to accommodate growth, network capacity is rapidly becoming the primary focus of the district's capex programme.

Operating expenditure

Operating expenditure is forecast to increase from $29.1 million (2024/25) to $36.6 million (2024/34) over the next ten years, an increase of 26%. The following chart shows the split between groups of activities for 2024/25.



The largest operating expenditure over the next ten years is on transportation ($91.3 million or 28%), followed by community services ($68.4 million 21%) water supply ($55.8 million or 17%) and wastewater ($50.5 million or 16%).

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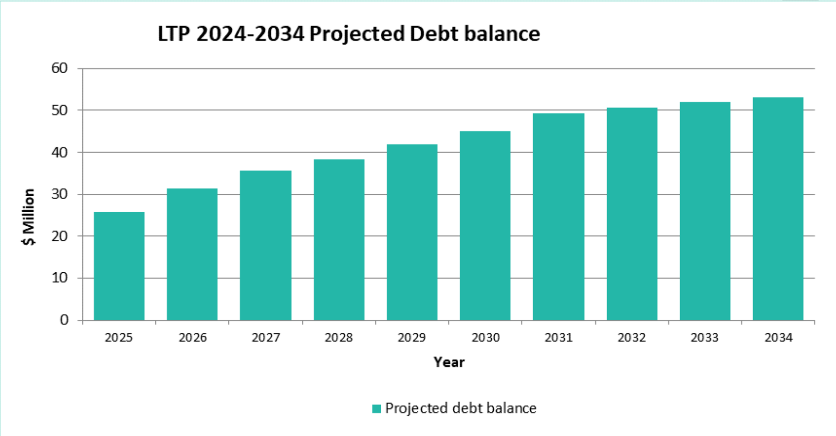
How we intend to finance our future

Borrowing

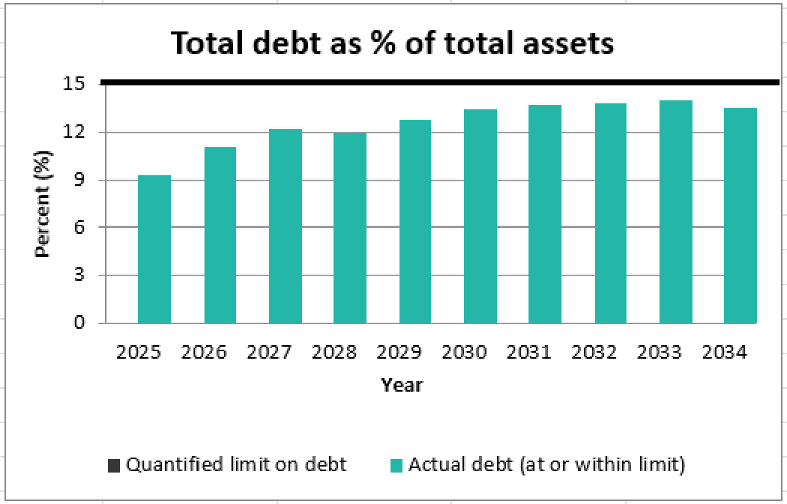
The Council has set prudential limits on the level of borrowing (debt) and the level of financing costs (interest). These are set out in its Treasury Management Policy. All three of the following conditions must be met:

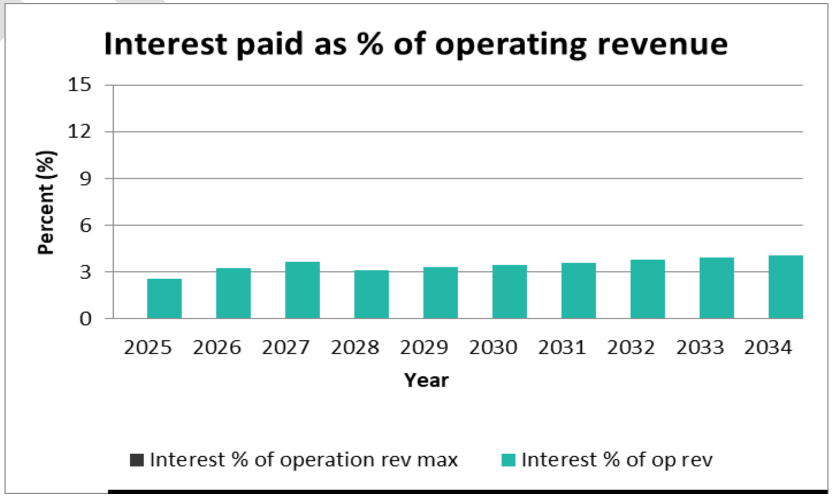
- total debt as a percentage of total assets will not exceed 15 percent
- in any financial year, gross interest paid on term debt will not exceed 12 percent of gross operating revenue
- in any financial year, gross interest expense will not exceed 50 percent net cash inflow from operating activities.

Debt rises from $25.7 million in 2024/25 to $53.0 million by 2033/34 over the next ten-year period to fund the capital works programme for our Infrastructure Strategy.



With the projected level of borrowing over the next ten years, these prudential benchmarks are set out in the following two graphs.
All are within the limits set by the Council.





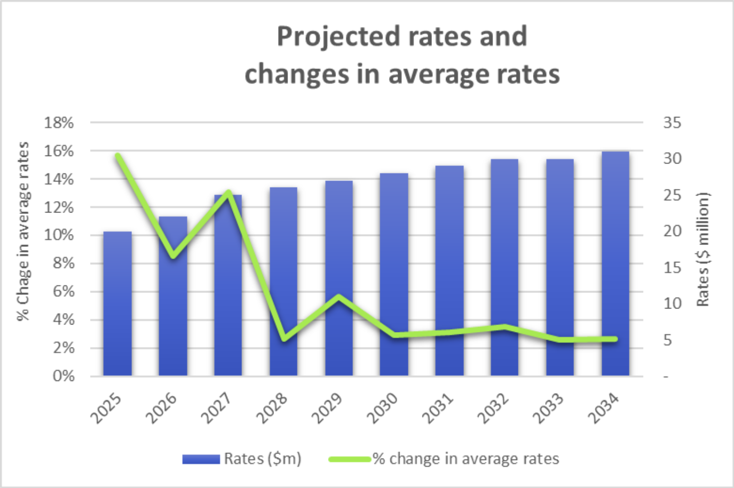
Rates

The purpose of local government is to enable democratic local decision-making and to meet its communities' needs for services—now and in the future. These responsibilities often create different views from the community and organisations on what the Council's priorities should be and how much money is spent.

Affordability is a concern for most ratepayers, whilst many feel that the Council should be doing more to accommodate the needs of a changing community. While grappling with this balancing act, the Council has taken into account as far as practicable the requirements of the current community without compromising future generations.

Rates limit

The following chart shows the projected rates during the Draft Long-Term Plan (the blue bars) and the percentage increase (the GREEN line) compared with the limit in rates increases (the grey line).

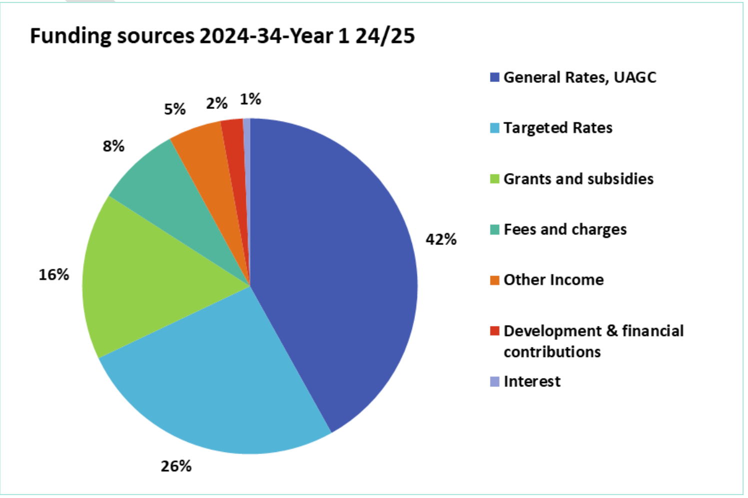


In the 2024/25 financial year, the Council proposes to collect $20.1 million in rates revenue. This is an increase of $2.5 million on the current financial year and equates to an increase of 15.6% in the average rates, 15.09 % after taking into account growth in the rating base.

Actual rates each year for individual properties will vary depending upon the targeted rates that are applicable, the differential rating category, and the valuation of each property.

Other funding sources

The graph below shows how the Council will fund the services and projects it will deliver to the community over the next ten years. Currently, the Council draws over two-thirds of its operating revenue from general and targeted rates because it does not have alternative revenue streams, such as significant financial investment funds or investments in corporate enterprises and has taken a fairly low risk approach to borrowing.



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Some of the detail

Inflation

The numbers in this Draft Long-Term Plan incorporate inflation as forecast by economics consulting company BERL.[1]

The New Zealand Inflation Rate as reported by Statistics NZ, has decreased to 4.7 percent in the fourth quarter December 2023 from 5.60 percent in the third quarter of 2023. The Inflation Rate in New Zealand is expected to be 4.30 percent by the end of this quarter, March 2024.

Depreciation

Depreciation is calculated on an annual basis to fund the renewal of existing assets over time. It is a major expense. It represents over a quarter of total operating expenditure. Charging depreciation each year spreads the cost of an asset over its useful life. Generally, depreciation is funded by income (including rates) in the same year that the depreciation is incurred. Funding of depreciation results in an increase in the Council's cash balance over the ten-year period of the Plan, held in depreciation reserves. These cash funds will earn interest and will provide funding towards the replacement of relevant infrastructure assets in the future.
In this Draft Long-Term Plan, the Council will fully fund the depreciation expense, except for the following:

- Roads and footpaths
- Events Centre building and fitout
- All loan-funded capital and renewals expenditure
- Three waters assets – year one at 50%, year two at 75%

This recognises that either we do not need to build up the full amount of funds for future replacement, or it would not be fair on the current generation of ratepayers.

Some of the capital construction of roads and footpaths is funded from subsidies received from the New Zealand Transport Agency (NZTA), and the capital construction of other assets was partly funded from external funding. Therefore, we do not need to build up the full amount of replacement funds.

In general, capital expenditure for the renewal of existing assets will be funded from depreciation reserves. However, if insufficient reserve funds are available, the expenditure may be funded by borrowing.

We need to borrow to fund other capital expenditure. This may be because insufficient funds have built up in the past in depreciation reserves, it is a new asset, or is a significant improvement to an existing asset (sometimes referred to as an increased level of service).

In these cases, the Council considers it would be unfair for the current generation of ratepayers to pay both the loan repayment (to fund the existing asset) and the depreciation (to fund its replacement). During the terms of the loans, rates will fund the principal repayment and interest expense, after which rates will fully fund the annual depreciation expense. At the end of the asset life, there will be some depreciation reserves built up to contribute to the replacement cost.

[1] Business and Economic Research Limited, September 2023.

Reserve funds

Some financial reserves operate to hold funds generated in one year and applied in another. The main sources of funds are depreciation, the setting aside of surpluses, and asset sales. The reserves are used to accumulate depreciation, to smooth income between years (for example, elections are every three years, and some funds are set aside in the two intervening years), for emergency or contingency funds, or to set aside some funding for special projects. Draw down is mainly for funding asset renewals.

Our policies allow for the internal borrowing from cash reserves, for which a market-based interest rate is charged.

Security on borrowing

The Council provides lenders with security on its borrowings through a debenture trust deed. This gives lenders a charge over Council's rates income. In the unlikely event of Council defaulting on a loan, the lender has the ability to ensure a rate is set to recover the outstanding amount owed. This security is attractive to lenders and helps ensure Council can obtain ongoing support for its debt programme and reduces the interest rate required by lenders.

Security may also be offered over specific assets with prior Council approval. The Council will offer security on infrastructure assets only where special rating provisions apply. It intends to continue to secure its borrowing in the current manner.

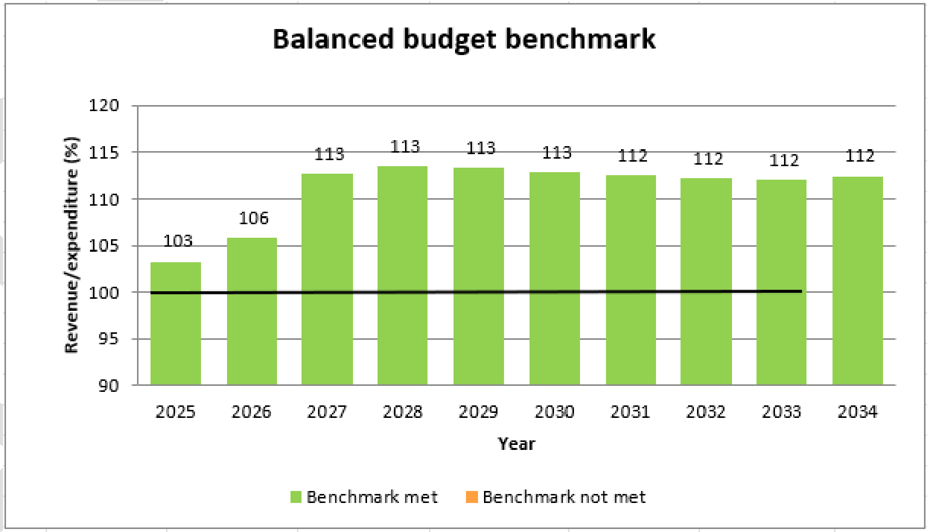
Balancing the budget

Under Section 100 of the Local Government Act 2002, the Council is required to ensure that it raises sufficient revenue to cover its projected operating expenses unless it considers it prudent not to do so.

The rates are set to cover:

- the net cost of the activity (expenses less any revenue)
- plus an amount to cover the repayment of loan principal, or to build up reserves for future year expenses (such as the three-yearly elections)
- less any expenses that don't need to be funded or the Council has chosen not to fund e.g. depreciation.

In every year of this Draft Long-Term Plan Council will run a surplus, i.e. the revenue including rates will be more than our expenses.



Financial investments and equity securities

An investment is an asset held by Council that provides service potential or future economic benefit to Council. Investments include property, ownership in Council related trading entities and financial assets. A financial asset is any asset that is cash or the contractual right to receive cash including financial investment instruments.

Council holds financial investments sufficient to match reserve accounts created by Council resolution and as a result of short-term cash flow surpluses. The Council recognises that as a responsible public authority, any investments that it does hold should be of a relatively low risk. It further recognises that lower risk generally means lower returns. Council aims to maximise investment income within a prudent level of investment risks. Council currently has money invested with banks in New Zealand. Council aims to achieve market rates for these investments.

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